

AMENDED IN ASSEMBLY JUNE 14, 2007

AMENDED IN ASSEMBLY JUNE 7, 2007

AMENDED IN ASSEMBLY APRIL 10, 2007

CALIFORNIA LEGISLATURE—2007–08 REGULAR SESSION

## ASSEMBLY BILL

**No. 1591**

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**Introduced by Assembly Member Ma**  
**(Coauthors: Assembly Members De Leon, Garcia, and Mullin)**

February 23, 2007

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An act to ~~amend Section 25128~~ *amend, repeal, and add Section 25128* of the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

### LEGISLATIVE COUNSEL'S DIGEST

AB 1591, as amended, Ma. The Corporation Tax Law: allocation and apportionment.

The Corporation Tax Law imposes taxes measured by income and, in the case of a business with income derived from, or attributable to, sources both within and without this state, apportions the income between this state and other states and foreign countries in accordance with a specified 4-factor formula, except as otherwise provided.

This bill, for taxable years beginning on or after January 1, ~~2007~~ *2008 and before January 1, 2022*, would allow a taxpayer that is a member of the apportioning trade or business, *or a subgroup thereof*, to elect, by contracting with the Franchise Tax Board, as provided, to apportion its business income to this state by utilizing one of the revised apportionment formulas, as specified.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

1     SECTION 1. Section 25128 of the Revenue and Taxation Code  
2     is amended to read:  
3     25128. (a) Notwithstanding Section 38006, all business income  
4     shall be apportioned to this state by multiplying the business  
5     income by a fraction, the numerator of which is the property factor  
6     plus the payroll factor plus twice the sales factor, and the  
7     denominator of which is four, except as provided in subdivision  
8     (b) or (c).  
9     (b) (1) If an apportioning trade or business derives more than  
10    50 percent of its “gross business receipts” from conducting one or  
11    more qualified business activities, all business income of the  
12    apportioning trade or business shall be apportioned to this state by  
13    multiplying business income by a fraction, the numerator of which  
14    is the property factor plus the payroll factor plus the sales factor,  
15    and the denominator of which is three.  
16    (2) For purposes of this section, a “qualified business activity”  
17    means the following:  
18    (A) An agricultural business activity.  
19    (B) An extractive business activity.  
20    (C) A savings and loan activity.  
21    (D) A banking or financial business activity.  
22    (c) (1) Notwithstanding any other provision of law, for taxable  
23    years beginning on or after January 1, ~~2007~~ 2008, and before  
24    January 1, 2022, a taxpayer that is a member of an apportioning  
25    trade or business may, on behalf of the apportioning trade or  
26    business or a subgroup thereof, elect to adjust, as provided in  
27    ~~paragraph (2), as provided in paragraph (3), to adjust~~ the fraction  
28    described in subdivision (a) or (b), as applicable, by utilizing one  
29    of the following alternative methods:  
30    (A) (i) In calculating its business income apportioned to this  
31    state, the apportioning trade or business, or a subgroup thereof,  
32    may add an additional sales factor to the numerator of the fraction  
33    described in subdivision (a) or (b), whichever is applicable, and  
34    may increase the denominator of that fraction by one for ~~each~~ every  
35    two hundred fifty million dollars (\$250,000,000) of qualified

1 expenditures made ~~on or after January 1, 2007~~. *during a taxable*  
2 *year beginning on or after January 1, 2008.*

3 (ii) The apportioning trade or business, or a subgroup thereof,  
4 must submit and certify, with each tax return filed with the  
5 Franchise Tax Board, a summary of the qualified expenditures.

6 (B) (i) The apportioning trade or business, or a subgroup  
7 thereof, may adjust the property factor and the payroll factor used  
8 in the fraction described in subdivision (a) or (b), whichever is  
9 applicable, as follows:

10 (I) ~~(aa)-(ia)~~ The value of real and tangible personal property  
11 ~~acquired or rented by the taxpayer on or after January 1, 2007, in~~  
12 ~~this state owned or rented by the taxpayer in a taxable year that~~  
13 ~~is in excess of the value of the taxpayer's real and tangible personal~~  
14 ~~property owned or rented and used in this state in the base year~~  
15 ~~and otherwise includable in the computations of the property factor,~~  
16 ~~as defined in Section 25129, shall be excluded from the numerator~~  
17 ~~of that property factor until the election is terminated.~~

18 ~~(ab)~~  
19 (ib) For purposes of this section, if real and tangible personal  
20 property acquired or rented by a taxpayer in this state in a taxable  
21 ~~year is disposed of by the taxpayer within one year or less of the~~  
22 ~~year is disposed of by the taxpayer in the following taxable year~~  
23 ~~and that disposition occurs within one year or less of the date the~~  
24 ~~property was first available for use in this state, placed in service,~~  
25 ~~then the value of that property shall be included in the numerator~~  
26 ~~of the taxpayer's property factor for such period that period. If the~~  
27 ~~return for such period has already been filed, an amended return~~  
28 ~~is required to be filed.~~

29 (II) ~~(aa)-(ia)~~ The amount of compensation paid in this state by  
30 the taxpayer, in a taxable year that is in excess of the amount of  
31 total compensation paid in this state in the base year and otherwise  
32 includable in the computations of the payroll factor, as defined in  
33 Section 25132, shall be excluded from the numerator of that payroll  
34 factor.

35 ~~(ab)~~  
36 (ib) For purposes of this section, "compensation in the base  
37 year" does not include extraordinary events such as deferred  
38 compensation payouts or stock option exercises.

39 ~~(ac) For purposes of this section, sales or other transactions~~  
40 ~~between members of an apportioning trade or business shall not~~

1 ~~be considered a qualified expenditure or new investment made in~~  
2 ~~this state.~~

3 (ii) The apportioning trade or business, or a subgroup thereof,  
4 must submit and certify, with each tax return filed with the  
5 Franchise Tax Board, a summary of the new investment made in  
6 this state.

7 (2) *For purposes of this subdivision, all of the following apply:*

8 (A) *Sales or other transactions among members of an*  
9 *apportioning trade or business shall not be taken into account for*  
10 *purposes of determining the amount of qualified expenditures*  
11 *incurred, or new investments made, by the trade or business, or a*  
12 *subgroup thereof, in this state.*

13 (B) *Amounts paid to acquire stock or other equity interests in*  
14 *a corporation or other business entity or an asset acquisition of*  
15 *an entire ongoing business operation are excluded from qualified*  
16 *expenditures.*

17 (C) *A subgroup making an election under paragraph (3) is*  
18 *prohibited from doing either of the following:*

19 (i) *Adding an additional sales factor under subparagraph (A)*  
20 *if the apportioning trade or business incurs a reduction in the level*  
21 *of the qualified expenditures compared to the prior year qualified*  
22 *expenditures certified by the subgroup.*

23 (ii) *Modifying its property or payroll factor, or both, under*  
24 *subparagraph (B), unless the amount of the apportioning trade or*  
25 *business' property or payroll, or both, in this state exceeds the*  
26 *amount of its property or payroll, or both, in this state in the*  
27 *immediately preceding taxable year.*

28 (D) *Only one subgroup of an apportioning trade or business*  
29 *may make an election allowed by paragraph (1).*

30 ~~(2)~~

31 (3) (A) On or after January 1, 2007, a taxpayer may elect to  
32 adjust the fraction described in subdivision (a) or (b), whichever  
33 is applicable. The election shall be made by attaching a statement  
34 to the original, timely filed return identifying the apportioning  
35 trade or business, or a subgroup thereof, specifying the method of  
36 adjusting the apportionment factor as described in subdivision (a)  
37 or (b), and designating the member of the apportioning trade or  
38 business, or a subgroup thereof, that will be required to submit  
39 and certify the information, as required by paragraph (1).

1 (B) The election may be terminated without the consent of the  
2 Franchise Tax Board after it has been in effect for at least 84  
3 months. The termination shall be made on an original, timely filed  
4 return for the first year in which the election is to be terminated.

5 (C) The election may be terminated before the 84-month period  
6 described in subparagraph (B) has elapsed either by the taxpayer,  
7 with the permission of the Franchise Tax Board, or by the Franchise  
8 Tax Board, if the taxpayer fails to submit a certification signed by  
9 an officer, as required by paragraph (1).

10 (D) The election shall remain in effect until terminated.

11 (E) This subdivision shall not be construed to terminate the  
12 water's-edge election made by a taxpayer pursuant to Section  
13 25113, nor shall it be construed to allow any change in, or  
14 adjustments to, that election.

15 (F) (i) *In the event the termination of the election occurs within*  
16 *the 84-month period, with the permission of the Franchise Tax*  
17 *Board, an apportioning trade or business, or subgroup thereof,*  
18 *shall be prohibited from making an election for the following 84*  
19 *months and any adjustment reported pursuant to paragraph (1)*  
20 *shall remain in effect for the years prior to termination.*

21 (ii) *In the event the termination of the election occurs after the*  
22 *84-month period, the adjustments reported by the apportioning*  
23 *trade or business, or a subgroup thereof, pursuant to paragraph*  
24 *(1), may be carried over until January 1, 2022. If an apportioning*  
25 *trade or business, or subgroup thereof, terminates an election after*  
26 *84 months, and then makes a new election, the prior adjustments*  
27 *reported pursuant to paragraph (1) remain in effect until January*  
28 *1, 2022.*

29 (G) (i) *If a new affiliate member is formed or acquired by an*  
30 *apportioning trade or business, or a subgroup thereof, or the*  
31 *apportioning trade or business, or a subgroup thereof is acquired,*  
32 *then the election made by the apportioning trade or business, or*  
33 *a subgroup thereof, pursuant to subparagraph (A), shall remain*  
34 *in effect unless the value of the new affiliate members' total*  
35 *business assets exceeds the value of the electing members' total*  
36 *business assets.*

37 (ii) *If the election is terminated as a result of either a formation*  
38 *or an acquisition, as described in clause (i), the provisions of*  
39 *subparagraph (F) shall not apply.*

40 (F)

1 (H) The Franchise Tax Board may prescribe any regulations  
2 that may be necessary or appropriate to implement the provisions  
3 of this subdivision.

4 (d) For purposes of this section:

5 (1) “Gross business receipts” means gross receipts described in  
6 subdivision (e) of Section 25120 (other than gross receipts from  
7 sales or other transactions within an apportioning trade or business  
8 between members of a group of corporations whose income and  
9 apportionment factors are required to be included in a combined  
10 report under Section 25101, limited, if applicable, by Section  
11 25110), whether or not the receipts are excluded from the sales  
12 factor by operation of Section 25137.

13 (2) “Agricultural business activity” means activities relating to  
14 any stock, dairy, poultry, fruit, furbearing animal, or truck farm,  
15 plantation, ranch, nursery, or range. “Agricultural business activity”  
16 also includes activities relating to cultivating the soil or raising or  
17 harvesting any agricultural or horticultural commodity, including,  
18 but not limited to, the raising, shearing, feeding, caring for, training,  
19 or management of animals on a farm as well as the handling,  
20 drying, packing, grading, or storing on a farm any agricultural or  
21 horticultural commodity in its unmanufactured state, but only if  
22 the owner, tenant, or operator of the farm regularly produces more  
23 than one-half of the commodity so treated.

24 (3) “Extractive business activity” means activities relating to  
25 the production, refining, or processing of oil, natural gas, or mineral  
26 ore.

27 (4) “Savings and loan activity” means any activities performed  
28 by savings and loan associations or savings banks which have been  
29 chartered by federal or state law.

30 (5) “Banking or financial business activity” means activities  
31 attributable to dealings in money or moneyed capital in substantial  
32 competition with the business of national banks.

33 (6) “Apportioning trade or business” means a distinct trade or  
34 business whose business income is required to be apportioned  
35 under Sections 25101 and 25120, limited, if applicable, by Section  
36 25110, using the same denominator for each of the applicable  
37 payroll, property, and sales factors.

38 (7) “Base year” means the year immediately preceding the year  
39 of election.

1 (8) “Value of real and tangible personal property” *in this state*  
2 means the value of owned and rented property as described in  
3 Section 25130.

4 (9) “Amount of compensation” means compensation described  
5 in Section 25132.

6 (10) “Subgroup” means a distinct group of affiliated  
7 corporations whose total business assets equal or exceed \$one  
8 billion dollars (\$1,000,000,000).

9 ~~(10) (A) “Qualified expenditures” means, in whole or in part,~~  
10 ~~all of the following expenditures:~~

11 (11) (A) “Qualified expenditures” means any of the following  
12 expenditures that are incurred on or after January 1, 2008:

13 (i) Capital expenditures, including maintenance costs, for real  
14 and tangible personal property located in this state.

15 (ii) Expenses incurred to acquire, develop, or license intellectual  
16 property in this state.

17 (iii) Research and development expenses, as defined in Section  
18 174 of the Internal Revenue Code, incurred in this state.

19 ~~(iv) Expenses incurred to develop, enhance, or maintain real~~  
20 ~~property and tangible personal property located in this state.~~

21 ~~(v)~~

22 (iv) Capitalized rent paid in this state in excess of the prior year.

23 ~~(vi) Compensation and benefits paid to employees in this state~~  
24 ~~in excess of the prior year.~~

25 ~~(vii) Payments to independent contractors and payroll companies~~  
26 ~~for work performed in this state in excess of the prior year.~~

27 (v) The total amount of compensation and benefits paid to  
28 employees in this state and the payments to independent  
29 contractors and payroll companies for work performed in this  
30 state in excess of the amount paid during the prior year.

31 ~~(viii)~~

32 (vi) Training costs incurred in this state.

33 ~~(ix)~~

34 (vii) Costs incurred in providing a basic level of health care to  
35 employees in this state, as defined in the Knox-Keene Act, in  
36 excess of the prior year.

37 ~~(x)~~

38 (viii) Expenditures incurred in connection with funding research  
39 at a four-year public or private college or university located in  
40 California.

~~(B) “Qualified expenditures” does not include amounts paid to acquire stock or other equity interests in a corporation or other business entity.~~

*(B) An expense that qualifies as an eligible expenditure under two or more categories of qualified expenditures, as listed in subparagraph (A), may be taken into account only under one category of qualified expenditures for purposes of satisfying the two hundred fifty million dollars (\$250,000,000) requirement described in subparagraph (A) of paragraph (1) of subdivision (c).*

~~(11)~~  
*(12)* In any case where the income and apportionment factors of two or more savings associations or corporations are required to be included in a combined report under Section 25101, limited, if applicable, by Section 25110, both of the following shall apply:

*(A)* The application of the more than 50 percent test of subdivision (b) shall be made with respect to the “gross business receipts” of the entire apportioning trade or business of the group.

*(B)* The business income of the apportioning trade or business, or a subgroup thereof, shall be apportioned in accordance with subdivision (a), (b), or (c), as applicable.

*(e)* The provisions of this section are severable. If any provision of this section or its application is held invalid, that invalidity shall not affect other provisions or applications that can be given effect without the invalid provision or application.

*(f)* The amendments made to this section by the act adding this subdivision shall apply to taxable years beginning on or after January 1, ~~2007~~ 2008.

*(g)* *This section shall remain in effect until December 1, 2002, and as of that date is repealed.*

*SEC. 2. Section 25128 is added to the Revenue and Taxation Code, to read:*

*25128. (a) Notwithstanding Section 38006, for taxable years beginning on or after January 1, 2022, all business income shall be apportioned to this state by multiplying the business income by a fraction, the numerator of which is the property factor plus the payroll factor plus twice the sales factor, and the denominator of which is four, except as provided in subdivision (b) or (c).*

*(b) If an apportioning trade or business derives more than 50 percent of its “gross business receipts” from conducting one or*



1 *more qualified business activities, all business income of the*  
2 *apportioning trade or business shall be apportioned to this state*  
3 *by multiplying business income by a fraction, the numerator of*  
4 *which is the property factor plus the payroll factor plus the sales*  
5 *factor, and the denominator of which is three.*

6 *(c) For purposes of this section, a “qualified business activity”*  
7 *means the following:*

8 *(1) An agricultural business activity.*

9 *(2) An extractive business activity.*

10 *(3) A savings and loan activity.*

11 *(4) A banking or financial business activity.*

12 *(d) For purposes of this section:*

13 *(1) “Gross business receipts” means gross receipts described*  
14 *in subdivision (e) of Section 25120 (other than gross receipts from*  
15 *sales or other transactions within an apportioning trade or*  
16 *business between members of a group of corporations whose*  
17 *income and apportionment factors are required to be included in*  
18 *a combined report under Section 25101, limited, if applicable, by*  
19 *Section 25110), whether or not the receipts are excluded from the*  
20 *sales factor by operation of Section 25137.*

21 *(2) “Agricultural business activity” means activities relating*  
22 *to any stock, dairy, poultry, fruit, furbearing animal, or truck farm,*  
23 *plantation, ranch, nursery, or range. “Agricultural business*  
24 *activity” also includes activities relating to cultivating the soil or*  
25 *raising or harvesting any agricultural or horticultural commodity,*  
26 *including, but not limited to, the raising, shearing, feeding, caring*  
27 *for, training, or management of animals on a farm as well as the*  
28 *handling, drying, packing, grading, or storing on a farm any*  
29 *agricultural or horticultural commodity in its unmanufactured*  
30 *state, but only if the owner, tenant, or operator of the farm*  
31 *regularly produces more than one-half of the commodity so treated.*

32 *(3) “Extractive business activity” means activities relating to*  
33 *the production, refining, or processing of oil, natural gas, or*  
34 *mineral ore.*

35 *(4) “Savings and loan activity” means any activities performed*  
36 *by savings and loan associations or savings banks which have*  
37 *been chartered by federal or state law.*

38 *(5) “Banking or financial business activity” means activities*  
39 *attributable to dealings in money or moneyed capital in substantial*  
40 *competition with the business of national banks.*

1 (6) “Apportioning trade or business” means a distinct trade or  
2 business whose business income is required to be apportioned  
3 under Sections 25101 and 25120, limited, if applicable, by Section  
4 25110, using the same denominator for each of the applicable  
5 payroll, property, and sales factors.

6 (7) Paragraph (4) of subdivision (c) shall apply only if the  
7 Franchise Tax Board adopts the Proposed Multistate Tax  
8 Commission Formula for the Uniform Apportionment of Net  
9 Income from Financial Institutions, or its substantial equivalent,  
10 and shall become operative upon the same operative date as the  
11 adopted formula.

12 (8) In any case where the income and apportionment factors of  
13 two or more savings associations or corporations are required to  
14 be included in a combined report under Section 25101, limited, if  
15 applicable, by Section 25110, both of the following shall apply:

16 (A) The application of the more than 50 percent test of  
17 subdivision (b) shall be made with respect to the “gross business  
18 receipts” of the entire apportioning trade or business of the group.

19 (B) The entire business income of the group shall be apportioned  
20 in accordance with either subdivision (a) or (b), as applicable.

21 (e) This action shall become operative on or after January 1,  
22 2022.

23 ~~SEC. 2.~~

24 SEC. 3. This act provides for a tax levy within the meaning of  
25 Article IV of the Constitution and shall go into immediate effect.

26 ~~SEC. 3.~~

27 SEC. 4. It is the intent of the Legislature that Section 1 of this  
28 act does not modify the sales factor, as defined in Section 25134  
29 of the Revenue and Taxation Code, used in any special  
30 apportionment formulas contained in the regulations promulgated  
31 by the Franchise Tax Board pursuant to Section 25137 of the  
32 Revenue and Taxation Code.